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UNCLAS BRASILIA 001048

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SUBJECT: BRAZIL MINIMUM WAGE DECISION REINFORCES LULA'S
FISCAL AUSTERITY

REF: BRASILIA 936

1. (U) The GoB announced April 29 that it would increase the minimum monthly wage to Reals 260 (about USD 88) from the current Reals 240 (reftel). The adjustment represents an increase in real terms of only 1.2%, despite considerable political pressure on the GoB for a significantly more substantial rise. To assuage critics that it is shortchanging the needy, the GoB also announced an increase (from Reals 13.48 to Reals 20 per child) in a government stipend targeted at families with an income less than one-and-a-half times the minimum wage. While the GoB's 2004 budget originally called for a minimum wage adjustment sufficient only to make up for inflation (i.e. to Reals 256.54), significantly higher than anticipated first quarter revenues give the GoB budgetary room for maneuver to cover the additional Reals 677.7 million cost over the remainder of this year without vitiating its primary surplus target (see septel on budget).

2. (U) The minimum-wage level has repercussions throughout federal, state and municipal budgets. While the federal government has comparatively few minimum-wage employees, the increase will have a big impact on state and municipal budgets, particularly in the northeast. Many of these municipalities reportedly lobbied for an increase no greater than that which was granted, saying they could afford no more. The problem at the federal level is the need to cover an increased deficit in the private-sector social-security pension system (INSS). The minimum pension level is linked to the minimum wage. A big factor here are the so-called "rural pensions," which granted INSS pensions, albeit at the minimum level, to many agricultural laborers or small farmers who never contributed to the system. The chart below illustrates the costs of the increase (which takes effect in June) for the remainder of 2004 and over the next twelve months.

Fiscal Impact of Minimum Wage
and Family Stipend Increase
(Millions of Reals)

	Jun-Dec 2004	Over next 12 months
Increase above budgeted level	3.46	3.46
Cost of each 1 Real Increase	141.23 m	214.70 m
Cost of minimum wage Increase	488.66 m	742.86 m
Cost of Family Stipend Increase	189.00 m	324.00 m
Grand Total	677.66 m	1,066.86 m

Source: CSFB

3. (SBU) This decision appears to have been difficult for Lula on a very personal level. He postponed the announcement several times and reportedly asked his economic team to review the numbers repeatedly to see if there was not wiggle room for a larger increase. While Lula had already acknowledged that his campaign pledge to double the minimum wage in real terms by the end of his term was simply not possible, his history of having been born into a poor family makes him feel in a very personal way the need to provide relief for low-income families. That the financial team won out on this issue illustrates yet again how deep Lula's commitment to fiscal responsibility has become.

HRINAK